Supreme Court, U.S.
FILED

961189 JAN 27 1997

OFFICE OF THE CLERK

In The

Supreme Court of the United States

October Term, 1996

BURLINGTON RESOURCES OIL & GAS COMPANY,

Petitioner,

vs.

FEDERAL ENERGY REGULATORY COMMISSION,

Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

PETITION FOR A WRIT OF CERTIORARI

RICHARD M. BLUMBERG
Associate General Counsel
BURLINGTON RESOURCES
OIL & GAS COMPANY
5051 Westheimer
Suite 1400
Houston, Texas 77056
(713) 624-9270

KIM M. CLARK
Counsel of Record
JOHN, HENGERER
& ESPOSITO
1200 17th Street, N.W.
Suite 600
Washington, D.C. 20036
(202) 429-8800

Attorneys for Petitioner

70391-B
(800) 3 APPEAL • (800) 5 APPEAL • (800) BRIEF 21
Lutz Appellate Services, inc.

39 pp

QUESTION PRESENTED

Whether under the service continuity provisions of Section 7(b) of the Natural Gas Act, 15 U.S.C. § 717f(b), it is an exercise of market and/or monopoly power for an interstate natural gas pipeline company to terminate transportation service unless an existing shipper pays the maximum agency-set rate, even though a lower competitive rate for such service has been established pursuant to an agency dictated right of first refusal bidding procedure.

PARTIES TO THE PROCEEDINGS BELOW

Federal Energy Regulatory Commission (Respondent)

Alabama Gas Corporation (Intervenor)

Algonquin Gas Transmission Company (Intervenor)

Allied Signal Inc. (Intervenor)

American Forest & Paper Association (Petitioner)

American Public Gas Association (Petitioner)

Amoco Production Company (Intervenor)

Anadarko Petroleum Corporation (Intervenor)

ANR Pipeline Company (Intervenor)

Arcadian Fertilizer (Petitioner)

Arco Natural Gas Marketing (Intervenor)

Arco Oil & Gas Company (Intervenor)

Arizona Electric Power Cooperative Inc. (Petitioner)

Arizona Public Service Company, *et al.* (Petitioner)

Asarco, Inc., Cyprus Miami Mining Corporation, and Magma Copper Company (Petitioner)

Associated Gas Distributors (Petitioner)

Associated Natural Gas Company (Petitioner)

Atlanta Gas Light Company (Petitioner)

Baltimore Gas & Electric Company (Petitioner)

Bay State Gas Company, *et al.* (Intervenor)

Board of Water, Gas & Light Commissioners, Albany, Georgia (Intervenor)

Brooklyn Union Gas Company (Intervenor)

Canadian Association of Petroleum Producers, *et al.* (Intervenor)

Carnegie Natural Gas Company (Petitioner)

Chattanooga Gas Company (Petitioner)

Cascade Natural Gas Corporation (Intervenor)

Chevron, U.S.A., Inc. (Intervenor)

Cincinnati Gas & Electric Company, *et al.* (Intervenor)

Citizens Gas & Coke Utility (Petitioner)

City of Hamilton, Ohio (Petitioner)

CNG Transmission Corporation (Petitioner)

Colorado Interstate Gas Company (Petitioner)

Colorado Springs Utilities (Petitioner)

Columbia Gas Distribution Companies (Intervenor)

Columbia Gas Transmission Corporation (Intervenor)

Conoco, Inc. (Intervenor)

Consolidated Edison Company of New York, Inc. (Petitioner)

Dakota Gasification Company (Intervenor)

Dayton Power & Light Company (Intervenor)

Destec Energy, Inc. (Intervenor)

East Ohio Gas Company, *et al.* (Intervenor)

East Tennessee Group (Petitioner)

East Tennessee Natural Gas Company (Intervenor)

Elizabethtown Gas Company, an Operating Division of NUI Corporation (Petitioner)

El Paso Natural Gas Company (Intervenor)

Enron Oil & Gas Marketing, Inc. (Intervenor)

Enserch Development Corporation (Petitioner)

Equitrans, Inc. (Petitioner)

Exxon Corporation (Intervenor)

Florida Cities (Intervenor)

Florida Gas Transmission Co. (Intervenor)

Foothills Pipelines Ltd. (Intervenor)

Fort Pierce Utilities Authority and the City of Vero Beach, Florida (Intervenor)

Fuel Managers Association (Intervenor)

Georgia Industrial Group (Petitioner)

Great Lakes Transmission Ltd. (Intervenor)

Hadson Gas Systems, Inc. (Petitioner)

Illinois Commerce Commission (Petitioner)

Illinois Power Company (Petitioner)

Indiana Gas Company (Petitioner)

Interstate Natural Gas Association of America (Intervenor)

Joint State Commissions and Consumer Advocates (Petitioner)

KN Energy, Inc. (Intervenor)

Kern River Gas Transmission Company (Petitioner)

Koch Gateway Pipeline Company (Petitioner)

Laclede Gas Company (Petitioner)

Long Island Lighting Company (Petitioner)

Louisville Gas & Electric Company (Petitioner)

Maryland Office of People's Counsel (Petitioner)

Maxus Exploration Company and Maxus Gas Marketing Company (Intervenor)

Memphis Light, Gas and Water Division (Petitioner)

Meridian Oil Inc. (Petitioner)

Michigan Consolidated Gas Company (Intervenor)

Midland Cogeneration Venture Limited (Petitioner)

Minnesota Public Utility Commission and Minnesota Department of Public Service (Intervenor)

Mississippi River Transmission Corporation (Intervenor)

Missouri and Kansas Gas Users (Intervenor)

Missouri Public Service Commission, *et al.* (Petitioner)

Mitchell Energy Corporation (Intervenor)

Mobile Gas Service Corporation, *et al.* (Intervenor)

Mobile Natural Gas, Inc. (Intervenor)

Montana Public Service Commission, Public Utilities Commission of South Dakota and Montana Consumer Counsel (Petitioner)

Mountaineer Gas Company (Petitioner)

National Association of State Utility Consumer Advocates (Petitioner)

National Association of Gas Consumers (Intervenor)

National Fuel Gas Supply Corporation (Intervenor)

Natural Gas Clearinghouse (Intervenor)

Natural Gas Pipeline Company of America (Intervenor)

New Jersey Board of Regulatory Commissioners (Petitioner)

New Jersey Natural Gas Company (Petitioner)

New York State Electric & Gas Corporation

New England Power Company (Petitioner)

Northern Indiana Public Service Company (Petitioner)

Niagara Mohawk Power Corporation (Petitioner)

NorAm Energy Corporation (Petitioner)

North Carolina Natural Gas Company and Public Service Commission of North Carolina (Intervenor)

Northeast Energy Associates and New Jersey Energy Associates (Intervenor)

Northern Border Pipeline Company (Intervenor)

Northern Distributor Group (Intervenor)

Northern States Power Company (Minn.), *et al.* (Intervenor)

Northern Natural Gas Company, *et al* (Intervenor)

Northwest Alaskan Pipeline Company (Petitioner)

Ocean State Power, *et al.* (Petitioner)

Office of the Consumers' Counsel, State of Ohio (Petitioner)

Orange and Rockland Utilities, Inc. (Petitioner)

Ozark Gas Transmission System (Petitioner)

Pacific Gas & Electric Company (Petitioner)

Pacific Interstate Transmission Company, *et al.* (Intervenor)

Pan-Alberta Gas, Ltd. (Intervenor)

Panhandle Customer Group (Intervenor)

Panhandle Eastern Pipe Line Company (Intervenor)

Panhandle Trading Company (Intervenor)

Pennzoil Exploration & Production Company and Pennzoil Gas Marketing Company (Intervenor)

PEPCO Energy (Petitioner)

Pennsylvania Office of Consumer Advocate (Petitioner)

Pennsylvania Public Utility Commission, *et al.* (Petitioner)

Peoples Gas System, Inc. (Intervenor)

Peoples Natural Gas Company (Petitioner)

Piedmont Natural Gas Company (Petitioner)

Philadelphia Electric Company (Petitioner)

Phillips Petroleum Company, *et al.* (Intervenor)

Plains Petroleum Operating Company (Petitioner)

Process Gas Consumers Group, *et al.* (Intervenor)

Producer-Marketing Transportation Group (Petitioner)

ProGas, Ltd. (Petitioner)

Public Service Commission of the Commonwealth of Kentucky (Petitioner)

Public Service Commission of Nevada (Intervenor)

Public Service Commission of the State of New York (Petitioner)

Public Service Commission of West Virginia, Consumer Advocate Division (Petitioner)

Public Service Commission of Wisconsin (Petitioner)

Public Service Electric & Gas Company (Intervenor)

Public Utilities Commission of the State of California (Petitioner)

Rochester Gas & Electric Company (Intervenor)

Shell Gas Trading Company (Intervenor)

South Jersey Gas Company (Intervenor)

South Carolina Pipeline Corporation (Intervenor)

Southern Natural Gas Company (Intervenor)

Southwest Gas Corporation (Petitioner)

State of Louisiana (Petitioner)

State of Indiana, Office of Utility Consumer Counselor (Petitioner)

Tenneco Gas, Inc. (Intervenor)

Tennessee Gas Pipeline Company (Intervenor)

Tennessee Small General Service and Columbia Small Customer Group (Intervenor)

Tennessee Valley Municipal Gas Association (Petitioner)

Texaco, Inc. (Intervenor)

Texas Eastern Transmission Corporation, *et al.* (Intervenor)

TransCanada Pipelines Limited (Intervenor)

Transcontinental Gas Pipe Line Corporation (Intervenor)

Transwestern Pipeline Company (Intervenor)

Trunkline Gas Company (Intervenor)

T.W. Phillips Gas & Oil Company (Intervenor)

UGI Utilities, Inc. (Intervenor)

Union Pacific Fuels, Inc. (Intervenor)

United Cities Gas Company (Intervenor)

United Distribution Companies (Petitioner)

Vastar Resources, Inc. and Vaster Gas Marketing, Inc. (Intervenor)

Virginia Electric & Power Company (Petitioner)

Washington Gas Light Company (Intervenor)

Williams Gas Marketing Company (Petitioner)

Williams Natural Gas Company (Petitioner)

Williston Basin Interstate Pipeline Company (Petitioner)

Windward Energy and Marketing Company (Intervenor)

Wisconsin Distributor Group (Petitioner)

PARENT COMPANIES AND NONWHOLLY OWNED SUBSIDIARIES

Burlington Resources Oil & Gas Company, successor to Meridian Oil Inc., is a Delaware corporation with its principal place of business in Houston, Texas. Burlington Resources Oil & Gas Company is a wholly owned subsidiary of Burlington Resources Inc. Burlington Resources Oil & Gas Company has no nonwholly owned subsidiaries.

TABLE OF CONTENTS

	Page
Question Presented	i
Parties to the Proceedings Below	ii
Parent Companies and Nonwholly Owned Subsidiaries	xii
Table of Contents	xiii
Table of Citations	xv
Opinions Below	1
Statement of Jurisdiction	1
Statute Involved	1
Statement of the Case	2
A. Regulatory Background	3
B. The Decision Below	4
Reasons for Granting the Writ	6
I. The court of appeals' decision conflicts with statutory protections for pipeline customers.	7
II. The court of appeals' decision endorses anti-competitive behavior and permits the exploitation of customers.	10

Contents

Page

III. Forcing a customer to pay the maximum rate or lose service is an exercise of market and/or monopoly power. 12

IV. The court below erred by applying Section 4 pipeline rate issues to a Section 7(b) abandonment procedure. 15

V. The court below erred by volunteering its own rationale for the agency decision. 18

Conclusion 20

Contents

Page

TABLE OF CITATIONS

Cases Cited:

American Gas Association v. Federal Energy Regulatory Commission, 912 F.2d 1496 (D.C. Cir. 1990), *cert. denied*, 498 U.S. 1084 (1991) 4, 7, 19

Associated Gas Distributors v. Federal Energy Regulatory Commission, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied*, 485 U.S. 1006 (1988) 14, 15, 16

Atlantic Refining Company v. Public Service Commission, 360 U.S. 378 (1959) 8, 9, 14

Burlington Truck Lines, Inc. v. United States, 371 U.S. 156 (1962) 19

California v. Southland Royalty Company, 436 U.S. 519 (1978) 8, 12

Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984) 19

Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1944) 8, 9, 14

Federal Power Commission v. Moss, 424 U.S. 494 (1976) 7

Federal Power Commission v. Natural Gas Pipeline Company, 315 U.S. 575 (1942) 16

Contents

	Page
Federal Power Commission v. Tennessee Gas Transmission Company, 371 U.S. 145 (1962)	16
Federal Power Commission v. Texaco, Inc., 417 U.S. 380 (1974)	13, 19
Jefferson Parish Hospital District No. 2 v. Hyde, 466 U.S. 2 (1984)	11
Maislin Industries, U.S., Inc. v. Primary Steel, Inc., 497 U.S. 116 (1990)	14
MCI Telecommunications Corporation v. American Telephone and Telegraph Company, 114 S. Ct. 2223 (1994)	19
Michigan Consolidated Gas Company v. Federal Power Commission, 283 F.2d 204 (D.C. Cir. 1960)	9
Mobil Oil Exploration & Producing Southeast, Inc. v. United Distribution Companies, 498 U.S. 211 (1991)	7
Moraine Pipeline Company v. Federal Energy Regulatory Commission, 906 F.2d 5 (D.C. Cir. 1990)	19
Permian Basin Area Rate Cases, 390 U.S. 747 (1968)	14
Public Service Commission v. Federal Energy Regulatory Commission, 813 F.2d 448 (D.C. Cir. 1987)	14

Contents

Page

Securities and Exchange Commission v. Chenery Corporation, 332 U.S. 194 (1947) 19, 20

Sunray Mid-Continent Oil Company v. Federal Power Commission, 364 U.S. 137 (1960) 8, 9, 12

Sunray Mid-Continent Oil Company v. Federal Power Commission, 239 F.2d 97 (10th Cir. 1956), *rev'd on other grounds*, 353 U.S. 944 (1957) 8, 9

Tarpon Transmission Company v. Federal Energy Regulatory Commission, 860 F.2d 439 (D.C. Cir. 1988) 19

United Distribution Companies, et al. v. Federal Energy Regulatory Commission, 88 F.3d 1105 (D.C. Cir. 1996) 1

United Gas Pipe Line Company v. Federal Power Commission, 385 U.S. 83 (1966) 9

United Gas Pipe Line Company v. McCombs, 442 U.S. 529 (1979) 9

Statutes Cited:

15 U.S.C. § 717f(b) (1994) ..... *passim*

15 U.S.C. § 717r(b) (1994) 1

28 U.S.C. § 1254(1) (1994) 1

Page

Other Authorities Cited:

Order No. 636, FERC Statutes & Regulations ¶ 30,939 (1992) ..... *passim*

Order No. 636-A, FERC Statutes & Regulations ¶ 30,950 (1992) ..... *passim*

Pipeline Service Obligations, and Revisions to Regulations Governing Self-Implementing Transportation Under Part 284 of the Commission's Regulations and Regulations of Natural Gas Pipelines After Partial Wellhead Decontrol, Order No. 636-B, 61 FERC ¶ 61,272 (1992) ..... *passim*

Secondary Market Transactions on Interstate Natural Gas Pipelines, 77 FERC ¶ 61,183 (1996) 11

Burlington Resources Oil & Gas Company (Burlington Resources)[1] (hereinafter "Petitioner") petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia in this case.

OPINIONS BELOW

The opinion of the court of appeals is reported at *United Distribution Companies, et al. v. Federal Energy Regulatory Commission*, 88 F.3d 1105 (D.C. Cir. 1996). Pet. App. 1a-174a.[2] The Federal Energy Regulatory Commission's (FERC or Commission) decisions reviewed by the court are reported at Order No. 636 (Pet. App. 175a-407a); the Commission's orders on rehearing are reported at Order No. 636-A (Pet. App. 408a-812a) and Order No. 636-B (Pet. App. 813a-1002a).

STATEMENT OF JURISDICTION

The judgment of the court of appeals was entered on July 16, 1996. Timely petitions for rehearing and rehearing *en banc* were denied on October 29, 1996. Pet. App. 1003a-1006a. The jurisdiction of the Court is invoked pursuant to 28 U.S.C. § 1254(1) (1994) and 15 U.S.C. § 717r(b) (1994).

STATUTE INVOLVED

Section 7(b) of the Natural Gas Act (NGA), 15 U.S.C. § 717f(b) (1994), provides in pertinent part that:

---

1. Burlington Resources is the successor — by virtue of a name change effective July 11, 1996 — to Meridian Oil Inc. (Meridian), which was a petitioner in the proceeding below. For purposes of continuity, the Burlington Resources name has been substituted for Meridian where that name was used in the proceedings below.

2. The several petitioners from the decision below are submitting a joint appendix. All references herein to the appendix are to that joint appendix.

> No natural-gas company shall abandon all or any portion of its facilities subject to the jurisdiction of the Commission, or any service rendered by means of such facilities, without the permission and approval of the Commission first had and obtained, after due hearing, and a finding by the Commission that the available supply of natural gas is depleted to the extent that the continuance of service is unwarranted, or that the present or future public convenience or necessity permit such abandonment.

STATEMENT OF THE CASE

This case presents an important new issue of administrative law which should be decided by the Supreme Court. That issue is whether it is lawful to force an existing utility customer to pay the maximum rate set by a regulatory agency for continued service, even though competitive forces which the agency stated would control and protect the customer's access to service establish a lower (and otherwise lawful) market value for the subject service.

The context of this question is the service continuity protections in Section 7(b) of the NGA (Pet. App. 1020a), which prevent an interstate natural gas pipeline company (pipeline) from terminating an existing transportation service without prior permission from FERC. As part of the Commission's Order Nos. 636, *et al.* rulemaking, a pipeline was given advance (*i.e.*, pregranted abandonment) authority to stop service to an existing customer, unless the customer matched the highest rate and best terms offered by another party. However, if the highest rate bid and then matched by the existing shipper was less than the maximum permissible rate, FERC allowed the pipeline to

terminate the existing service unless the existing shipper agreed to pay that rate.

The court below upheld FERC, finding — without citation to any precedent — that the NGA protects a customer's right to continued transportation service only if the customer pays the maximum rate. The NGA, however, was intended by Congress, and has been interpreted by this Court, to protect the rights of consumers against the monopolistic practices of natural gas pipeline utilities. But forcing a customer to pay the maximum rate or lose its service rights aids, not protects against, the exercise of market and/or monopoly power by a pipeline. This is in direct conflict with the consumer protections guaranteed by Section 7(b) of the NGA.

A. Regulatory Background

Section 7(b) of the NGA protects the right of existing shippers on interstate natural gas pipelines to retain their right to service unless and until FERC permits abandonment of such service. Abandonment may be granted in advance of the termination of the underlying contract of service (*i.e.*, pre-granted abandonment), provided the circumstances required in the statute are found to be present when the pre-granted abandonment determination is made.

In Order No. 636, FERC exercised its authority to provide for pre-granted abandonment under NGA Section 7(b) where service contracts of more than one year were due to expire. In the rulemaking, the existing shipper was able to retain its service rights by matching the highest rate and best terms offered by other interested parties. Pet. App. 312a-323a . FERC thus elected to have market forces determine which customers would have access to interstate pipeline capacity when an existing contract for firm transportation service expired. The right of first refusal

(ROFR) procedure was developed by FERC in response to the remand of an earlier unsuccessful attempt to fashion pregranted abandonment procedures. *American Gas Association v. FERC* (*AGA*), 912 F.2d 1496 (D.C. Cir. 1990), *cert. denied*, 498 U.S. 1084 (1991).

On rehearing of its initial order in the Order No. 636 series, FERC clarified that if the best bid was at a price less than the FERC-set maximum rate, the pipeline could decline to enter into a new or extended service agreement. Therefore, even though the existing customer had agreed to pay the highest rate bid for the service, the Commission's rule permitted the pipeline to cease service. FERC's rationale for this action was that the pipeline would not be compelled to discount its service (hereafter the no discounting rule). Pet. App. 637a.

In response to objections by Burlington Resources and others that the no discounting rule was inconsistent with FERC's assertions that market forces should allocate capacity, and with long-standing Section 7(b) protections for existing customers, FERC merely restated that pipelines would not be required to discount. Pet. App. 929a-937a. The Commission also asserted that if a pipeline failed to maximize throughput (*i.e.*, by leaving capacity unsold), there was no guarantee the pipeline would be able to recover all its costs in its next rate case. Pet. App. 936a.

B. The Decision Below

The D.C. Circuit Court (D.C. Circuit or court below) affirmed FERC's refusal, as part of the ROFR procedures, to insist that a pipeline renew the service of an existing shipper who was willing to match the highest bid for the subject capacity, if that bid was at less than the maximum rate. The court found that FERC had protected against the pipeline's exercise of market power by removing the pipeline's ability to influence the bidding,

and by limiting the maximum rate the pipeline could charge. Pet. App. 54a-55a.

The court noted that the purpose of selective discounting by a pipeline was to increase throughput by attracting volumes it might not otherwise transport. Thus, Burlington Resources'

> proposal that pipeline's be required to discount in favor of demand-inelastic, captive customers would render meaningless pipeline's ability to charge up to the maximum approved rate. The § 7(b) abandonment provisions protect customers against loss of service only if the customer is willing to pay the maximum rate approved in a rate proceeding.

Pet. App. 55a.

The court also responded to the contention that the ability of a pipeline to refuse service at less than the maximum rate prevented the ROFR mechanism from reflecting competitive market forces. The D.C. Circuit found adequate FERC's assertion that a pipeline which declined to discount its service in favor of not contracting for available capacity might not be entitled to full cost recovery in its next rate case. According to the court, this was a sufficient incentive for the pipeline to discount in appropriate circumstances. Pet. App. 55a-56a.

The D.C. Circuit denied a timely petition for rehearing and suggestions for rehearing *en banc* filed by other Petitioners with respect to another issue in the Order No. 636 rulemaking. Pet. App. 1003a-1006a.

REASONS FOR GRANTING THE WRIT

The decision below conflicts with the fundamental purpose of the Natural Gas Act, as understood and interpreted by this Court, which is to use regulation as a means to protect consumers by maintaining service continuity and by preventing pricing abuse due to the exercise of market and/or monopoly power by interstate pipelines. Contrary to these statutory standards, the court below sustained FERC's election to sacrifice the interests of pipeline customers, the persons for whom the NGA was enacted, in order to advance the revenue maximization of regulated pipelines.

FERC's no discounting rule, therefore, is inconsistent with the consumer protections in Section 7(b) of the Natural Gas Act. The best illustration of this failing is the rationale offered by the court below, which is that if the pipeline were required to accept a market-determined rate, it would be unable to force "demand-inelastic, captive customers" to pay the maximum permissible rate. It is difficult to conceive a more perverse analysis of a statutory provision which was designed to protect consumers.

FERC's no discounting rule thus results in the unusual situation whereby the regulator supports and promotes the ability of a regulated entity to exercise market and/or monopoly power to the detriment of the utility's customers. Whether that is a permissible or appropriate policy under the NGA appears to be a matter of first impression for this Court.

I.

THE COURT OF APPEALS' DECISION CONFLICTS WITH STATUTORY PROTECTIONS FOR PIPELINE CUSTOMERS.

FERC's ROFR mechanism is intended to comply with the requirements for pregranted abandonment under Section 7(b). *See, e.g., FPC v. Moss*, 424 U.S. 494 (1976). *See also Mobil Oil Exploration & Producing Southeast, Inc. v. United Distribution Companies*, 498 U.S. 211 (1991). In fact, the ROFR mechanism in Order No. 636 is a direct response to the Commission's failure to comply with this requirement in an earlier rulemaking. In *AGA*, *supra*, the D.C. Circuit remanded FERC's effort at pregranted abandonment in order for the Commission to reconsider

> how pregranted abandonment trumps another basic precept of natural gas regulation — protection of gas customers from pipeline exercise of monopoly power through refusal of service at the end of a contract period.

912 F.2d at 1518.

The ROFR mechanism, however, fails to meet the service continuity and rate protection concerns inherent in Section 7(b). The court below sought to reconcile this contradiction by finding that a shipper was assured of retaining its transportation service only by paying the maximum rate. However, the D.C. Circuit did not offer a single case reference to support this proposition. Moreover, this holding directly contradicts numerous decisions of this Court to the effect that the purpose of the NGA is consumer protection, not pipeline revenue maximization.

The NGA has been determined by this Court to be a consumer-oriented statute. As noted in *FPC v. Hope Natural Gas Company*, 320 U.S. 591, 610 (1944), "[t]he primary aim of this legislation was to protect consumers against exploitation at the hands of natural gas companies."

> We cannot find in the words of the Act or in its history the slightest intimation or suggestion that the exploitation of consumers by private operators through the maintenance of high rates should be allowed to continue. . . .

Id. at 612. *See also* the Court's summary of the purpose of the NGA in *California v. Southland Royalty Company*, 436 U.S. 519, 523 (1978), "[t]he fundamental purpose of the Natural Gas Act is to assure an adequate and reliable supply of gas at reasonable prices." *See also Atlantic Refining Company v. Public Service Commission (CATCO)*, 360 U.S. 378, 388 (1959), where the Court noted that the NGA was framed "to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges."

Section 7(b) of the NGA protects consumers against unwarranted termination of service by requiring prior Commission approval of the abandonment of service. *See Sunray Mid-Continent Oil Company v. FPC (Sunray II)*, 364 U.S. 137, 143 (1960), where this Court stated that Section 7(b) protects against the interruption of service, so there is regulation of "the great economic power of the pipeline companies as compared with that of communities seeking natural gas service." Moreover, "[n]o single factor in the Commission's duty to protect the public can be more important to the public than the continuity of service furnished." *Sunray Mid-Continent Oil Company v.*

FPC, 239 F.2d 97, 101 (10th Cir. 1956), *rev'd on other grounds*, 353 U.S. 944 (1957).[3]

This Court on several occasions has addressed the importance of continuity of service under Section 7(b). *See, e.g.*, *CATCO*, *supra*; *Sunray II*, *supra*, *see also*, *United Gas Pipe Line Company v. FPC*, 385 U.S. 83 (1966), where the Court held that United's refusal to take gas after the expiration of the contract term constituted an abandonment under Section 7(b) (*id.* at 86), because the transportation of gas in interstate commerce is a service covered by that provision (*id.* at 87). *See also United Gas Pipe Line Company v. McCombs*, 442 U.S. 529, 538 (1979), quoting from *Sunray II*, 364 U.S. at 158 n.25 (1960), "[w]e have consistently recognized that the Commission's 'legal control over the continuation of service' . . . is a fundamental component of the regulatory scheme."

If the finding of the court below that a customer must pay the highest possible rate in order to retain its service is upheld, then the consumer protections built into the NGA, as interpreted by this Court in *Hope*, *CATCO*, and the other decisions cited above, have no practical meaning. Continuity of service and protection from unreasonable rates are required to go hand-in-hand under the NGA, but that is not the case under the ROFR mechanism. Continuity of service is not maintained where a pipeline may terminate an existing service unless the shipper is

---

3. *See Michigan Consolidated Gas Co. v. FPC*, 283 F.2d 204, 214 (D.C. Cir. 1960).

> The fact that abandonment of public service requires Government approval symbolizes the special legal status and obligations of common carriers and public utilities. This includes an obligation, deeply embedded in the law, to continue service.

willing to pay the highest possible rate, even though that customer is willing to pay the highest competitive rate bid.

II.

THE COURT OF APPEALS' DECISION ENDORSES ANTI-COMPETITIVE BEHAVIOR AND PERMITS THE EXPLOITATION OF CUSTOMERS.

Under the ROFR mechanism set up by FERC, competition was supposed to allocate pipeline capacity. As FERC explained,

> [t]he criteria established for pregranted abandonment for long-term transportation contracts of long-term firm transportation will foster competition and economic efficiency, and streamline the administrative process, while protecting the legitimate needs of many customers for continued service.

Pet. App. 319a. In addition, FERC claimed the ROFR procedure would: (i) allow "the rate to play a role in rationing capacity . . . ." (Pet. App. 323a); (ii) "recognize the role of market forces in determining contract price and term" (Pet. App. 675a); and (iii) permit "the market to determine contract terms" and allow "market forces to play a significant role in determining the contract price. . . ." Pet. App. 933a.

These noble pronouncements, however, were rendered meaningless due to the no discounting rule. In practice, market factors will not be allowed to have any effect on the disposition of capacity, since the pipeline is not obligated to contract for service at less than the maximum rate. This chasm between the announced purposes of FERC's ROFR mechanism and what actually occurs under that procedure was ignored by the court below.

In fact, the ROFR mechanism allows market forces to apply only where demand exceeds supply, a situation which benefits the pipeline by allowing it to sell its services at the maximum rate. If, however, the supply of pipeline capacity exceeds the demand,[4] market forces are rendered irrelevant and the shipper must pay the maximum rate, which is a situation that also benefits the pipeline. Thus, FERC's ROFR mechanism is anti-competitive, since it forces a customer to pay a rate for continued service which exceeds the market value of that service.

This is an obvious use of regulatorily sanctioned market power to exploit utility customers.[5] Moreover, compelling a customer to pay a non-competitive rate is patently inconsistent with FERC's basic rationale for establishing the ROFR bidding mechanism, which was to let market forces determine contract terms. Pet. App. 319a, 675a, 933a.

Pipeline customers who accept the cost burdens associated with firm transportation service (*i.e.*, paying monthly demand charges for capacity access whether the capacity is used or not)

---

4. The amount of interstate pipeline capacity exceeds the demand for service in the nation's largest natural gas market, California. FERC made the following finding concerning the California gas market in *Secondary Market Transactions on Interstate Natural Gas Pipelines*, 77 FERC ¶ 61,183 at 61,707 (1996).

> [T]here is significant excess capacity available throughout California. Total interstate capacity into California currently exceeds demand by 2.0 Bcf/d. . . . [E]vidence . . . shows the capacity is trading at less than maximum rates.

Footnotes omitted.

5. *See, e.g., Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 27 n. 46 (1984), where this Court defined market power to exist "whenever prices can be raised above the levels that would be charged in a competitive market."

do so in order to assure themselves of guaranteed service of the highest priority. This is a particularly acute concern for captive shippers, especially those who have their own service obligations at the local level (*e.g.*, local distribution companies).[6] These customers strive for service continuity at the lowest possible rates. *See California, supra.*

FERC's no discounting rule, however, creates a conflict between these two statutorily recognized policies. Either the shipper can preserve its transportation service by paying a rate which exceeds market value (and which later may be deemed excessive and thus possibly unrecoverable by state or local regulators), or the shipper can forego guaranteed pipeline service and take the risk of meeting its customer demands through less secure means. That Hobbesian choice, however, is not consistent with the intent of the NGA, or with the holdings of this Court.

III.

FORCING A CUSTOMER TO PAY THE MAXIMUM RATE OR LOSE SERVICE IS AN EXERCISE OF MARKET AND/OR MONOPOLY POWER.

Before the court below, Petitioner argued that forcing an existing shipper to pay the maximum rate in order to retain service was an exercise of monopoly power where the market value of the service was less than the maximum rate. The court

---

6. This Court noted the importance of the reliance by local communities on natural gas service as far back as *Sunray II*, 364 U.S. at 143 (1960):

> If the pipeline company were left free to cease its service to the local distribution company, a local economy which had grown dependent on natural gas as a fuel would be at its mercy.

below disagreed, noting that the ROFR mechanism restricted the pipeline's exercise of market power "by limiting the maximum rate that the pipeline may charge." Pet. App. 55a. The D.C. Circuit also based its conclusion on an earlier discussion in its opinion.

> If the existing customer is willing to pay the maximum approved rate, then the right-of-first-refusal mechanism ensures that the pipeline may not abandon the certificated service.

Pet. App. 49a.

This finding, however, fails to address specifically whether forcing a customer to pay the highest permissible rate set by a regulatory agency is an exercise of market power by a regulated utility where competition — and the ROFR procedure — fixes a lower value for the subject service. This appears to be a question of first impression for this Court.

Regulation by the FERC of the interstate transportation of natural gas is a legislative substitute for open competition made necessary by the natural monopoly positions of gas pipelines. *See, e.g., FPC v. Texaco, Inc.*, 417 U.S. 380, 397-8 (1974), where the Court noted:

> It is abundantly clear from the history of the Act and from the events that prompted its adoption that Congress considered that the natural gas industry was heavily concentrated and that monopolistic forces were distorting the market price for natural gas.

Footnote omitted.

Under the NGA, FERC establishes pipeline rates within a zone of reasonableness. *Public Service Commission v. FERC*, 813 F.2d 448, 451 (D.C. Cir. 1987), *citing Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968). Thus, for each pipeline service in the tariff there appears a small minimum rate and a significantly higher maximum rate; both these rates — and all rates in between — are deemed just and reasonable. *Associated Gas Distributors v. FERC (AGD)*, 824 F.2d 981, 1007 (D.C. Cir. 1987), *cert. denied*, 485 U.S. 1006 (1988). Consequently, if the pipeline were to renew an existing service at a market-determined price that was less than the maximum, that rate would be both lawful and just and reasonable.[7] FERC's ROFR mechanism, however, requires payment of the maximum rate or the loss of service.

There is nothing in the NGA or the decisions of this Court that compels a natural gas shipper to pay the maximum possible rate for transportation service. In fact, the decisions in *Hope* and *CATCO*, *supra*, compel the opposite conclusion in order to protect consumers from exploitation by pipeline monopolists. In addition, since FERC itself sets rates within a fairly wide zone of reasonableness, the highest rate has no better claim to being just and reasonable than any other rate within the range of reasonableness. Moreover, there is nothing in Section 7(b) which mandates a tie-in between service continuity and payment of the highest possible rate.

If a natural gas pipeline can force its customer to pay an above-market price for service, that is an exercise of market

7. It is undisputed that a rate less than the maximum is lawful, since any rate negotiated by the parties between the FERC-established minimum and maximum rates that appear in the pipeline tariff is permissible without a specific filing with FERC. Consequently, the ruling in *Maislin Industries, U.S., Inc. v. Primary Steel, Inc.*, 497 U.S. 116 (1990), against the legality of a negotiated but unpublished rate that was less than the filed rate under the Interstate Commerce Act does not apply.

and/or monopoly power.[8] The fact that the rate being imposed on the customer is government sanctioned does not make it any less excessive. The effect on the customer is the same; the customer incurs costs that would not be possible in a competitive environment, and which should not be permitted in a regulatory environment.

IV.

THE COURT BELOW ERRED BY APPLYING SECTION 4 PIPELINE RATE ISSUES TO A SECTION 7(b) ABANDONMENT PROCEDURE.

The basis for the D.C. Circuit's affirmance of FERC's no discounting rule was to insure full cost recovery by the pipeline through its ability to constrain captive customers to pay the highest possible rate in order to continue their transportation service. *See, e.g.*, the D.C. Circuit's reference to the need for a pipeline to extract the maximum rate from its "demand-inelastic, captive customers." Pet. App. 55a. Pipeline cost recovery, however, is a Section 4 rate matter, not a Section 7(b) issue.

Even if pipeline cost recovery were relevant under Section 7(b), the FERC and the D.C. Circuit erred in asserting that a guarantee of pipeline cost recovery is an axiom of the NGA. In

---

8. *See. e.g.*, *AGD*, 824 F.2d at 1010-1 (D.C. Cir. 1987),

> [P]ipeline transportation service is marked by a degree of natural monopoly. . . . In such an industry, "value-of-service" ratemaking (*i.e.*, rates varying on the basis of differing demand characteristics) has an established place, though not an uncontested one.

Footnotes omitted.

fact, pipelines are not guaranteed full cost recovery under the NGA, merely the opportunity to do so. *See, e.g., FPC v. Natural Gas Pipeline Company*, 315 U.S. 575, 590 (1942). "[T]he hazard of not making a profit remains on the company. . . ." *FPC v. Tennessee Gas Transmission Company*, 371 U.S. 145, 152 (1962). Moreover, there was no evidence cited by the court below to support its hypothesis that discounting service to firm transportation customers necessarily would lead to an inability of a pipeline to recover its cost of service. In fact, the D.C. Circuit made just the opposite finding in its review of the predecessor of Order Nos. 636, *et al.* with respect to the possible rate effects of discounting. *See AGD*, 824 F.2d at 1012.

The court below also should have taken into account that setting pipeline rates on a cost-of-service basis is not an exact science. For example, if a pipeline can lower its costs of operation or obtain additional throughput once the rates are set, it can earn a greater profit than anticipated in the ratemaking process. Thus, selling capacity to an existing shipper at less than the maximum rate does not, contrary to the opinion below, necessarily render meaningless the ability of the pipeline to earn its cost of service and/or charge the maximum rate.

In addition, the D.C. Circuit relied on FERC's assertion that if a pipeline failed to maximize throughput by withholding its capacity rather than selling it at a discount, the pipeline might not be able to recover all its costs in the next rate case. Pet. App. 936a. Neither FERC nor the court below explained, however, how this "threat" of future agency action resolved the immediate dilemma of an existing shipper who must either agree to a new service contract at an above-market rate or lose its transportation service.

Moreover, the D.C. Circuit also failed to address other deficiencies in the purported value of this "threat" by FERC.

For example, FERC's threat is not stated as a certainty, and thus it may prove meaningless in an actual pipeline rate case.[9] And, even if the "threat" were taken seriously, the pipeline still might elect to hold its capacity for future sale rather than undergo a review of all its rates in a new Section 4 rate case. The timing of a rate filing is an important factor ignored by the court below, since it is the pipeline and not FERC who controls when a Section 4 rate case will be filed. Finally, if a pipeline really jeopardized its opportunity for full cost recovery by not discounting when market factors dictate, there would be no reason for FERC's no discounting rule in the first place.

In addition, the court below failed to coordinate its holding on the no discounting rule with its decision to reverse and remand the requirement that ROFR renewals could be for a term of up to 20 years. Pet. App. 49a-53a. As conceived by FERC, the ROFR consisted of paying the highest lawful rate and agreeing to a contract term of up to 20 years. A commitment of that

---

9. The D.C. Circuit described FERC

> as **assuring** that a pipeline is not entitled to full cost recovery in its next rate proceeding when it forgoes the opportunity to recover some of its fixed costs from a bid rate between the minimum and maximum filed rates.

Emphasis added, footnoted omitted; Pet. App. 55a. In fact, what FERC stated was:

> [I]f a pipeline fails to attempt to maximize throughput, there is no guarantee that it will be able to recover all the cost of its underutilized capacity from its customers when it files its next rate case.

Footnote omitted; Pet. App. 936a.

duration at a discounted rate might have been the reason FERC refused to require discounting, had FERC given a reason, however the 20-year term requirement has been reversed and remanded, with the indication that a much shorter term might be more appropriate.

At the time of the filing of this writ, FERC has not acted on the remand. However, if FERC amends its rules to provide for a much shorter contract term, the possible adverse effects on the pipeline of an ROFR discount will be reduced, thereby removing an obstacle to letting the market-determined rate apply to ROFR service renewal, and thus allowing a firm transportation customer to continue its service at the highest market-determined price.

V.

THE COURT BELOW ERRED BY VOLUNTEERING ITS OWN RATIONALE FOR THE AGENCY DECISION.

FERC repeatedly states as part of its ROFR mechanism that pipelines will not be required to discount their service. Pet. App. 637a, 936a. However, FERC never once explained why this is proper, despite requests to do so in the rulemaking process, and despite its recognition that the market value of pipeline capacity may be less than the maximum rate.

> If customers were able to renew service at less than the maximum rate, . . . this would merely be reflective of the competitive market. If no one bids at the maximum rate, that would mean that the capacity is valued at less than the maximum rate. However, pipelines are not required to discount under

> the rule and are not required to accept any offer at less than the maximum rate.

Pet. App. 673a.

The fact that the agency failed completely to explain a fundamental tenet of its decision should have been a sufficient basis to reverse this finding for a lack of reasoned decisionmaking. *See, e.g., AGA*, 912 F.2d at 1516-8; *Moraine Pipeline Company v. FERC*, 906 F.2d 5 (D.C. Cir. 1990); *Tarpon Transmission Company v. FERC*, 860 F.2d 439, 445 (D.C. Cir. 1988).

The court below, however, proceeded to provide its own rationale for FERC's no discounting rule. It was the court below, not FERC, who opined that discounting under the ROFR mechanism must be prohibited in order for pipelines to maximize their revenues from captive customers and thus avoid a purported cost underrecovery, and that abandonment could be avoided only if the existing shipper agrees to pay the maximum rate.[10]

Substituting the court's judgment and reasoning for that of the agency is directly contradictory to the fundamental principle of administrative law that an agency order must stand or fall on what the agency said. *FPC v. Texaco, Inc.*, 417 U.S. at 397; *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168-9 (1962); *SEC v. Chenery Corporation*, 332 U.S. 194, 196

---

10. In this instance, there is no question of giving deference to the agency's interpretation of its enabling statute under *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), since it was the court below, not FERC, who rendered this view of Section 7(b). Moreover, "an agency's interpretation of a statute is not entitled to deference when it goes beyond the meaning that the statute can bear", *MCI Telecommunications Corp. v. American Telephone and Telegraph Co.*, 114 S. Ct. 2223, 2231 (1994).

(1947). Here, FERC said nothing to support its no discounting rule. Therefore, the court below erred in not reversing and remanding for the purpose of having FERC provide a rationale for its decision.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

KIM M. CLARK
Counsel of Record
JOHN, HENGERER & ESPOSITO
1200 17th Street, N.W.
Suite 600
Washington, D.C. 20036
(202) 429-8800

RICHARD M. BLUMBERG
Associate General Counsel
BURLINGTON RESOURCES OIL & GAS COMPANY
5051 Westheimer
Suite 1400
Houston, Texas 77056
(281) 878-3700

Attorneys for Petitioner